[JOINT COMMITTEE PRINT]

DESCRIPTION OF MISCELLANEOUS TAX BILLS

LISTED FOR A HEARING

BEFORE THE

SUBCOMMITTEE ON TAXATION AND DEBT MANAGEMENT GENERALLY

OF THE

COMMITTEE ON FINANCE

ON JUNE 24, 1980

PREPARED FOR THE USE OF THE

COMMITTEE ON FINANCE

BY THE STAFF OF THE

JOINT COMMITTEE ON TAXATION

JUNE 20, 1980

U.S. GOVERNMENT PRINTING OFFICE
63-904 O WASHINGTON : 1980 JCS-31-80

CONTENTS
26
27
28
29
30
31

CONTENTS

CONTENTS
26
27
28
29
30
31

INTRODUCTION

The bills described in this pamphlet have been scheduled for a hearing on June 24, 1980, by the Senate Finance Subcommittee on Taxation and Debt Management Generally. There is one bill that has been passed by the House of Representatives (H.R. 5391) and 10 Senate bills (S. 1614, S. 2075, S. 2493, S. 2547, S. 2646, S. 2660, S. 2757, S. 2766, S. 2783, and S. 2784) described in the pamphlet.

The first part of the pamphlet is a summary of the bills presented in bill numerical order. This is followed by a more detailed description of the bills, setting forth present law, the issues involved, an explanation of the bills, the effective dates, and the estimated revenue effects.

I. SUMMARY

1. H.R. 5391

Second Tier Tax Correction Act of 1980

Under present law, a two-tier excise tax system is applicable to private foundations, employee benefit trusts, and black lung benefit trusts, with respect to prohibited acts of these organizations. The second-tier excise tax is not imposed if the prohibited act is corrected within a correction period. The Tax Court has held that it lacks jurisdiction to redetermine a deficiency for a second-tier tax because the tax is not imposed until after its decision is final.

Under the bill, the second-tier excise tax would be imposed before any litigation begins (in order to insure that the Court will have jurisdiction) but would be forgiven if the prohibited act is corrected within a correction period.

2. S. 1614—Senator Bentsen

Local Newspaper Exemption From Foundation Business Holding Provisions

Under present law, private foundations are limited in their percentage ownership in a business enterprise. The bill would exempt holdings in an independent local newspaper business from these restrictions.

3. S. 2075—Senator Gravel

Definition of An Affiliated Group for Purposes of the Air Transportation Excise Taxes

Present law provides an exception from the air passenger ticket and air freight waybill excise taxes for air transportation provided by a member of an affiliated group of corporations to another member of the affiliated group, where the aircraft so used is not available for hire by persons who are not members of the affiliated group. The noncommercial aviation fuels taxes apply for fuel used in such instances.

The bill would expand the definition of an affiliated group to also include a tax-exempt labor organization and its tax-exempt trusts (and any wholly-owned corporations of such trusts) established for the sole and exclusive benefit of the members of such labor organization and their families and dependents.

4. S. 2493—Senator Glenn

Extension of Time for Payment of Manufacturers Excise Tax on Tires, Inner Tubes, and Tread Rubber

Under present law, an excise tax is imposed upon the sale of certain tires, inner tubes, and tread rubber by the manufacturer, producer, or importer. This tax generally is payable soon after such items are sold.

The bill would allow manufacturers, producers, and importers of taxable tires, inner tubes, and tread rubber to postpone payment of the excise tax upon the sale of items until 90 days after the last day of the month in which the item was sold.

5. S. 2547—Senators Gravel, Hatfield, Levin, and Hayakawa

Tax Exemption for Industrial Development Bonds for Beverage Container Facilities

Under present law, tax-exempt industrial development bonds (IDBs) may be used to provide solid waste disposal facilities. The term "solid waste" is defined by Treasury regulations to mean garbage, refuse or other discarded materials which have no market or other value at the place they are located.

Refillable beverage containers do not, in general, qualify as solid waste. As a result, tax-exempt financing is generally not available for facilities used in the collection and processing of such containers.

The bill would allow tax-exempt IDBs to be used to finance the acquisition of beverage container facilities for use in a State or locality that has enacted a law which requires a deposit on the bottles, discourages the sale of beverages in nonreturnable bottles, or prohibits or discourages the sale of beverages in metal container without nondetachable opening devices. The facilities that may be financed under the bill are:

(1) refillable beverage containers;

(2) property used in the collection, sorting or handling of beverage containers;

(3) property used in the cleaning and processing of refillable beverage containers; and

(4) property used for the manufacture of metal beverage container tops with nondetachable opening devices.

6. S. 2646—Senator Boren

Save America Savings Account Act of 1980

Under present law, an individual may exclude from gross income up to $200 ($400 on a joint return) of dividends and interest received in calendar years 1981 and 1982. (For 1980 and years after 1982, the exclusion is for up to $100 of dividends for each individual.)

The bill would allow an additional exclusion for qualified interest received on deposits held for not less than one year of up to $100,000 where the deposits are used to make loans for the purchase of owner-occupied residential property, the operation of a trade or business, or the operation of a farm for farming purposes. The rate of interest on the deposit may not exceed 7 percent and the rate of interest on the loan may not exceed the rate of interest on the deposit by more than 2½ percentage points.

7. S. 2660—Senator Moynihan

Tax Exemption for Industrial Development Bonds for Facilities for the Local Furnishing of Gas

Under present law, tax-exempt industrial development bonds (IDBs) may be used to provide facilities for the local furnishing of gas. Such a facility is defined as property for the furnishing of gas which is part of a system providing service to the general populace in a service area comprising no more than two contiguous counties. The bill would amend the definition of facilities for the local furnishing of gas to include property for the furnishing of gas which is part of a system providing service to the general populace in a service area comprised of a city and one contiguous county.

8. S. 2757—Senators Bentsen, Stevenson, Heinz, and Danforth

Taxation of Export Trading Companies

In the case of a Domestic International Sales Corporation (DISC) which is also an export trading company (as defined in the companion bill, the Export Trading Company Act of 1980 (S. 2718)), the bill would expand the definition of qualifying DISC income to include the export of certain U.S. services and the performance of services which facilitate the export of U.S. goods and services. The bill would also allow a banking organization which invests in the voting stock of an export trading company to qualify as a DISC.

Under present law, a subchapter S corporation may not have corporate shareholders and may not derive more than 80 percent of its gross receipts from foreign sources. Under the bill, a subchapter S corporation which is also an export trading company may have corporate shareholders as long as they qualify as subchapter S corporations. Also under the bill, such dual status corporations are exempt from the foreign income limitation.

9. S. 2766—Senator Gravel

Tax Exemption for Industrial Development Bonds for Facilities the Primary Purpose of Which Is the Generating of Hydroelectric Power

Under present law, tax-exempt industrial development bonds (IDBs) may be used to provide financing for the installation of electrical generating equipment at, and the rehabilitation of, an existing dam. Tax-exempt IDBs may also be used to provide financing for the installation of electrical generating equipment at a site which does not involve the impoundment of water. However, in order to qualify for tax-exempt financing, the facility must have an installed capacity of less than 125 megawatts, the facility must be owned for tax purposes by a State or local government, and the facility must satisfy the "public use" requirement.

The bill would allow tax-exempt IDBs to be used to provide facilities the primary purpose of which is the generating of hydroelectric power.

10. S. 2783—Senators Wallop and Garn

Definition of Shale Oil Equipment for the Energy Investment Credit

In addition to the generally applicable 10-percent investment tax credit, the Energy Tax Act of 1978 provided a 10-percent energy investment credit for shale oil equipment. The latter credit applies to equipment for producing or extracting shale oil from shale rock, but generally not to equipment for use in upgrading the extracted liquid.

The bill would expand the definition of shale oil equipment to include equipment used to upgrade shale oil.

S. 2784—Senator Gravel

Effective Date of the Energy Investment Credit for Coke Ovens

Under the Crude Oil Windfall Profit Tax Act of 1980, the 10-percent energy investment credit for alternative energy property was extended to equipment used to produce coke and coke gas for periods after December 31, 1979.

Under the bill, the credit for equipment used to produce coke and coke gas would apply retroactively with respect to periods after September 30, 1978 (the general effective date for the Energy Tax Act of 1978, under which the energy tax credit was enacted).

II. DESCRIPTION OF BILLS

1. H.R. 5391

Second Tier Tax Correction Act of 1980

Present law

Under present law, the Internal Revenue Code contains nine sections which impose a two-tier excise tax system to insure the compliance of private foundations [1] pension trusts [2] and black lung benefit trusts [3] with certain provisions of the Code. Under each of the sections, a first-tier excise tax is imposed automatically if the foundation or trust engages in a prohibited act (such as self dealing between a disqualified person and a private foundation), and a much larger second-tier excise tax is imposed for failing to correct the prohibited act within a "correction period." The "correction period" ends after the time a court decision as to whether the taxpayer is liable for the second-tier tax becomes final. This system is designed to provide an adequate opportunity for court review and correction of the transaction before the Internal Revenue Service can impose the second-tier tax. The second-tier taxes are intended to be sufficiently high to compel voluntary compliance (at least after court review) with these provisions.

In a recent case,[4] the Tax Court held that it lacked the authority to redetermine a deficiency of a second-tier tax with respect to an act of self dealing by a private foundation under Code section 4941(b). The Court found that because the second-tier tax is not "imposed" until after its decision is final, it did not have jurisdiction to redetermine a deficiency of that tax. In addition, the Court noted that the "amount involved" (upon which the amount of tax is based) cannot be determined until after the decision has become final.

Issue

The issue is whether the two-tier excise tax system for prohibited acts by private foundations, pension trusts, and black lung trusts

---

[1] The provisions relating to private foundations are Code sections 4941 (self-dealing), 4942 (failure to distribute income), 4943 (excess business holdings), 4944 (jeopardy investments), and 4945 (taxable expenditures). These provisions were added by the Tax Reform Act of 1969.

[2] The provisions relating to pension trusts are Code sections 4971 (minimum funding) and 4975 (prohibited transactions). These provisions were added by the Employee Retirement Income Security Act of 1974.

[3] The provisions relating to black lung benefit trusts are Code sections 4951 (self-dealing) and 4952 (taxable expenditures). These provisions were added by the Black Lung Benefits Revenue Act of 1977.

[4] *Adams* v. *Commissioner*, 72 T.C. 81 (1979). This decision was followed in two subsequent cases: *Larchmont* v. *Commissioner*, 72 T.C. 131 (1979), and *H. Fort Flowers Foundation* v. *Comissioner*, 72 T.C. 399 (1979).

should be amended in order to insure the courts have jurisdiction to enforce the second-tier taxes.

Explanation of the bill

Under the bill, the second-tier excise tax would be imposed at the end of the taxable period (i.e. the time the Internal Revenue Service mails a notice of deficiency to the taxpayer with respect to the first-tier tax or when the first-tier tax is assessed if no deficiency notice is mailed). However, the second-tier tax would not be assessed if the taxpayer files a petition with the Tax Court to redetermine that tax and the taxpayer corrects the prohibited act by the end of the correction period. Under the bill, the correction period would end when the decision of the Tax Court becomes final (under Code sec. 7481), except that it would be extended by any period the IRS determines is reasonable and necessary to bring about correction (Code sec. 4962(e)).

The bill also would provide for a supplemental proceeding by the Court to determine whether the taxpayer corrected the prohibited act within the correction period, if the Court previously determined that the second-tier tax was properly imposed.

Thus, where the taxpayer petitions the Tax Court to redetermine a second-tier tax, the tax would not be assessed unless the Court decides either in reviewing imposition of the tax, or in a supplemental proceeding on the timeliness of a correction, that the taxpayer has engaged in an act giving rise to a first-tier tax and that the act was not timely corrected.

In refund cases, the bill would suspend the collection of any second-tier excise tax which was assessed (for example, because a notice of deficiency was mailed and no petition was filed with the Tax Court) until the taxpayer completes its administrative and judicial refund procedures. Thus, a taxpayer may obtain U.S. district court or Court of Claims review of issues involving the second-tier tax without first being required to pay the second-tier tax.[5]

Finally, the bill would fix the amount of the second-tier taxes on self-dealing (Code sec. 4941, 4951, and 4975) on the date the second-tier tax is imposed.

(An identical bill, S. 2485, was introduced by Chairman Russell B. Long.)

Effective date

The bill would apply to second-tier taxes assessed after the date of enactment of the bill (except in cases where a court decision with respect to that tax is final on that date).

Revenue effect

The bill is not expected to have any effect on budget receipts.

---

[5] Under Treasury regulations, the correction period is extended during the pendency of refund proceedings. Under Code section 7422(g)(1), the jurisdiction requirement that a taxpayer pay the second-tier tax is waived.

2. S. 1614—Senator Bentsen

Local Newspaper Exemption From Foundation Business Holdings Provision

Present Law

The Tax Reform Act of 1969 imposed an excise tax upon the excess business holdings of a private foundation (Code sec. 4943). Generally, under the excess business holdings provisions, the combined ownership of a business by a private foundation and all disqualified persons cannot exceed 20 percent of the voting stock of the business (35 percent if other persons have effective control of the business).

The 1969 Act provided that, if a private foundation and disqualified persons together had holdings on May 26, 1969, in excess of the permitted amounts under the general rules, then those holdings could be retained if they consisted of not more than 50 percent of the business. If the combined holdings exceeded 50 percent of the business on that date, then over a transitional period the combined holdings have to be reduced to 50 percent (ultimately to 35 percent if the disqualified persons hold, in the aggregate, no more than 2 percent of the business; if they hold more than 2 percent, then the combined holdings may continue to be as much as 50 percent, of which the foundation itself may hold no more than 25 percent).

Issue

The issue is whether ownership by a private foundation in an independent local newspaper business should be exempted from the excess business holdings provision of present law.

Explanation of the bill

The bill provides that an independent local newspaper business would not be treated as a business enterprise for purposes of the excess business holdings provision (Code sec. 4943). Thus, there would be no limitation on the percentage interest in such an enterprise that a foundation may own.

An independent local newspaper business means a business (whether organized as a corporation, partnership, or proprietorship), no interests in which are traded in an established securities market, which publishes an independent local newspaper. An "independent local newspaper" is defined as a newspaper publication which is not a member of a "chain of newspaper publications" and which has all of its publishing offices in a single city, community or metropolitan area, or, as of January 1, 1979, within one State. A "chain of newspaper publications" is defined as two or more newspaper publications under common control on January 1, 1979, and which are not published in a single city, community, or metropolitan area.

The principal beneficiary of this bill is Houston Endowment, Inc., which owns the Houston Chronicle. However, it is expected that other taxpayers owning newspapers would benefit from enactment of the bill.

Effective date

The bill would apply to taxable years ending after the date of enactment of the bill.

Revenue effect

It is estimated that the bill would reduce income tax liability by $10 million per year. After approximately five years, it is estimated that the bll would reduce estate tax liability by $100 million per year. There would be a negligible impact in fiscal year 1981.

3. S. 2075—Senator Gravel

Definition of an Affiliated Group for Purposes of the Air Transportation Excise Taxes

Present law

The excise taxes on air passenger tickets (under Code sec. 4261)[1] and air freight waybills (under Code sec. 4271)[2] apply to commercial aviation, that is, as a business of transporting persons or property for compensation or hire by air.

Code sections 4281 and 4282 provide two exceptions to the air passenger and air freight taxes. Code section 4281 provides that the taxes do not apply to transportation by an aircraft having a maximum take-off weight of 6,000 pounds or less, except when the aircraft is operated on an established line. Code section 4282 provides for an exception for certain air transportation provided for other members of an affiliated group. This exception is applicable for air transportation provided by a member of an affiliated group[3] to another member of the affiliated group where the aircraft so used is not available for hire by persons who are not members of the affiliated group.

The aviation fuels taxes for noncommecrial aviation (under Code sec. 4041(c)) apply in such instances where the transportation taxes do not apply.

Issue

The issue is whether the affiliated group exception from the air transportation excise taxes for controlled corporations should be expanded to include a tax-exempt labor organization and exempt trusts (or corporations owned by the trust) established for the sole and exclusive benefit of the members of such labor organizations and their families and dependents.

Explanation of the bill

The bill would expand the affiliated group exception from the air transportation excise taxes for controlled corporations to also include

---

[1] The air passenger ticket tax presently is 8 percent through June 30, 1980, and 5 percent beginning on July 1, 1980. However, legislation is currently pending (H.R. 7477 as passed by the House of Representatives on June 17, 1980) to extend the 8-percent rate through September 30, 1980. The Finance Committee, on June 10, 1980, approved the substance of the 3-month extension. In addition, a Ways and Means Committee amendment, to be offered to H.R. 6721, would extend the 8-percent rate through September 30, 1982, and at 5 percent thereafter.

[2] The air freight waybill tax presently is 5 percent through June 30, 1980, and is scheduled to expire on July 1, 1980. However, H.R. 7477 would extend the present 5-percent tax through September 30, 1980. In addition, the Ways and Means Committee amendment to H.R. 6721 would extend the 5-percent tax through September 30, 1985.

[3] "Affiliated group" is a group of corporations connected through common stock ownership (as defined in Code sec. 1504(a), except that, for purposes of the transportation tax exception, all such corporations are treated as the includible corporation, without any exclusion under Code sec. 1504(b)).

tax-exempt labor organizations (under Code sec. 501) and their tax-exempt trusts (and any wholly-owned corporations of such trusts) established for the sole and exclusive benefit of the members of such labor organization and their families and dependents.

Effective date

The bill would be effective upon the date of enactment.

Revenue effect

This bill is estimated to have an insignificant revenue effect.

4. S. 2493—Senator Glenn

Extension of Time for Paying Excise Tax on Tires, Inner Tubes, and Tread Rubber

Present law

Under present law, a manufacturers excise tax is imposed upon the sale of certain tires, inner tubes and tread rubber (Code sec. 4071).

Under Code section 6302(a), the mode and time for collecting all manufacturers excise taxes is established by Treasury Regulations. Under the regulations generally applicable to the payment of manufacturers excise taxes (Treas. Regs. sec. 48.6302(c)-1), if an individual's liability for taxes reportable on a quarterly excise tax return (Form 720) exceeds $100 for any calendar month (other than the last month of a calendar quarter), then the amount of such liability must be deposited at an authorized depository, or at the Federal Reserve Bank serving the area in which the individual is located, on or before the last day of the month following the month for which the liability exceeds $100. In the case of the last month of a calendar quarter (and where the taxes for the quarter are less than $100), the taxes must be paid by the last day of the month following the close of the calendar quarter.

If an individual's liability for taxes reportable on a quarterly excise tax return exceeded $2,000 for any month in the preceding calendar quarter, then taxes for the following quarter (regardless of amount) must be deposited on a semi-monthly basis. Taxes which are payable semi-monthly must be deposited by the 9th day following the semi-monthly period to which the taxes relate. Generally, a semi-monthly period means the first 15 days of a calendar month or the portion of a calendar month following the 15th day of the month. Thus, taxes for the first 15 days of a calendar month must be paid by the 24th of that month, and taxes for the period after the 15th of a calendar month must be paid by the 9th of the following month.

In addition, if the semi-monthly period is within either of the first two months of the quarter, any underpayment of excise taxes for a month must be deposited by the 9th day of the second month following the month of the underpayment. Underpayments in the third month of the quarter must be deposited by the end of the first month after the end of the quarter.

The regulations contain no special rules to defer payment of the excise tax with respect to items sold on credit. However, Code section 4216(c) provides that, in the case of an installment sale and title does not pass until some future date, the tax is paid as installments are received.

Issue

The issue is whether the payment of the manufacturers excise tax on tires, inner tubes, and tread rubber should be delayed until 90 days after the end of the month in which the item is sold, i.e., for up to 4 months after a sale of and payment for the article.

Explanation of the bill

The bill would eliminate the Secretary's general regulatory authority, under Code section 6302(a), as to the payment of the excise tax imposed on tires, inner tubes, and tread rubber, by providing that such tax is payable 90 days after the last day of the month in which the manufacturer, producer, or importer sells taxable articles.

Effective date

The provisions of the bill would apply to tires, inner tubes, and tread rubber sold on or after the first month beginning after the date of enactment.

Revenue effect

It is estimated that this bill would reduce budget receipts by $190 million in fiscal year 1981 and by less than $5 million annually thereafter. (The fiscal year 1981 estimate is based on the assumption that this bill would be enacted after August 31, 1980.)

5. S. 2547—Senators Gravel, Hatfield, Levin, and Hayakawa

Tax Exemption for Industrial Development Bonds for Beverage Container Facilities

Present law

Under present law, interest on State and local government obligations is generally exempt from Federal income tax. However, since 1968, tax exemption has been denied to State and local government issues of industrial development bonds (IDBs). A State or local government bond is an IDB if (1) all or a major portion of the proceeds of the issue are to be used in any trade or business of a person other than a State or local government or tax-exempt organization, and (2) payment of principal or interest is secured by an interest in, or derived from payments with respect to, property or borrowed money used in a trade or business.

An exception to the denial of tax exemption for interest on IDBs applies in the case of IDBs which are used to provide solid waste disposal facilities. Solid waste disposal facilities are defined in Treasury regulations as property used for the collection, storage, treatment, utilization, processing, or final disposal of solid waste. A facility which disposes of solid waste by reconstituting, converting, or otherwise recycling it into material which is not solid waste will qualify as a solid waste disposal facility if 65 percent of the material introduced into the recycling process is solid waste (Treas. Reg. sec. 1.103–(f)(2)(ii)).

The Internal Revenue Code does not define the term "solid waste." However, the legislative history of the IDB exception for solid waste disposal facilities indicates that the term has the same meaning as it had in the Solid Waste Disposal Act. In that Act, solid waste was defined as "garbage, refuse, and other discarded solid materials." The legislative history of that Act states that "solid wastes include a great variety of things that individuals, manufacturers, commercial establishments, and communities discards as no longer useable."

The Treasury Regulations, which define the term "solid waste", provide that solid waste means garbage, refuse, and other discarded materials so long as it is property which is useless, unused, unwanted, or discarded solid material which has no market or other value at the place it is located (Treas. Reg. sec. 1.103–8(f)(2)(ii)).

As a result of the existing definition of the term "solid waste", facilities used in connection with returnable beverage containers will not, in general, qualify as solid waste disposal facilities.

Issue

The issue is whether tax-exempt IDBs should be allowed to be used to finance the acquisition of refillable beverage containers, property used in the collection, sorting, or handling of beverage containers, property used in the cleaning and processing of refillable beverage containers, and property used for the manufacture of metal beverage container tops with nondetachable openings in States or localities which prohibit or discourage the use of nonreturnable bottles or metal containers without nondetachable opening devices.

Explanation of the bill

The bill provides that interest on IDBs used to provide qualified beverage container facilities would be exempt from Federal income taxation. Beverage container facilities covered by the bill are: (1) the initial supply of refillable beverage containers and shells and (2) any facility used by a distributor or bottler of beverages (a) in the collection, sorting, or handling of beverage containers,[1] (b) in the cleaning and processing of refillable beverage containers, or (c) for the manufacture of metal beverage container tops with nondetachable opening devices.

A beverage container facility would be treated as a qualified beverage container facility where three requirements are met. First, the construction, reconstruction, erection, or acquisition of the facility must occur during the two-year period beginning on the effective date of a "beverage container law." Second, the facility must not replace an existing beverage container facility. Finally, the facility must be used in connection with a "beverage container law."

The bill defines a "beverage container law" as a law which (1) requires the purchaser of beverages sold in containers to pay a deposit or fee to the seller in connection with the purchase of such beverages, (2) prohibits or discourages the sale of beverages in nonreturnable containers, or (3) prohibits or discourages the sale of beverages in metal containers unless the containers have nondetachable opening devices.

Effective date

The bill would apply to obligations issued after December 31, 1979. In addition, the bill would allow the refinancing of existing conventionally financed beverage container facilities where (1) a bond resolution was adopted or other similar official action was taken by the issuer prior to the commencement of the construction, erection, or acquisition of the facility, and (2) the obligations are issued no later than one year after the date of enactment.

Revenue effect

It is estimated that this bill would reduce budget receipts by $10 million in fiscal year 1981, $20 million in 1982, $40 million in 1983, $60 million in 1984, and $70 million in 1985.

---

[1] This provision apparently is not restricted solely to refillable beverage containers. Thus, tax-exempt financing may be available under the bill with respect to this type of equipment which is used in conjunction with "throw-away" bottles and cans.

6. S. 2646—Senator Boren

Save America Savings Account Act of 1980

Present law

In calendar years 1981 and 1982, an individual may exclude from gross income up to $200 of dividend and interest income ($400 on a joint return) (Code sec. 116). The exclusion for dividends, which has been in the Code since 1954, generally applies to dividends paid by domestic corporations.[1] The exclusion for interest was enacted in the Crude Oil Windfall Profit Tax Act of 1980 and applies generally to most domestic sources of interest income.

Issue

The issue is whether an additional exclusion from gross income should be provided for interest received on deposits which are used to make loans for specifically designated purposes (i.e., for home ownership, trade or business, or farming purposes) where the rate of interest on the deposit does not exceed a designated amount (i.e., 7 percent) and the lower interest rate is flowed through to the borrower.

Explanation of the bill

Under the bill, amounts received as qualified interest for the taxable year would be excluded from gross income. The exclusion would not apply to interest income received with respect to amounts on deposit in excess of $100,000 for the taxable year. The amounts excluded from gross income under this proposal would be in addition to any amounts excludable under present law (Code sec. 116).

Qualified interest is defined as interest which is paid at a rate of 7 percent or less, but only if the principal on which the interest is earned (1) is held on deposit for not less than 1 year and (2) is used for the purpose of making qualified loans.

A qualified loan is a loan made for (1) the purchase of owner-occupied residential property, (2) the operation of a trade or business, or (3) the operation of a farm for farming purposes. The rate of interest payable on a qualified loan could not be more than 2½ percentage points above the rate of interest paid on the deposits from which the loan is made.

A qualified loan is not a loan used, in whole or in part, for the purchase of land, other than for the purchase of owner-occupied residential property.

Effective date

The bill would apply with respect to taxable years beginning after December 31, 1979.

[1] For 1980 and years after 1982, the general exclusion is for up to $100 of dividends received by an individual. Married couples filing joint returns may exclude up to $200 of dividends (up to $100 for each person).

Revenue effect

It is estimated that the bill would reduce calendar year liability and fiscal year receipts as follows:

(Millions of dollars)

	1980	1981	1982	1983	1984	1985
Calendar	10, 360	11, 603	12, 996	14, 555	16, 302	18, 258
Fiscal	[1]	12, 100	12, 787	14, 438	16, 302	17, 036

[1] Less than $5 million.

7. S. 2660—Senator Moynihan

Tax Exemption for Industrial Development Bonds for Facilities for the Local Furnishing of Gas

Present law

Under present law, interest on State and local government obligations is generally exempt from Federal income tax. However, since 1968, tax exemption has been denied to State and local government issues of industrial development bonds (IDBs). A State or local government bond is an IDB if (1) all or a major portion of the proceeds of the issue are to be used in any trade or business of a person other than a State or local government or tax-exempt organization, and (2) payment of principal or interest is secured by an interest in, or derived from payments with respect to, property or borrowed money used in a trade or business.

An exception to the denial of tax exemption for Interest on IDBs applies in the case of IDBs which are used to provide exempt activity facilities. Such facilities include facilities for the local furnishing of electric energy and gas (Code sec. 103(b) (4) (E)).

A facility for the furnishing of electric energy or gas is defined in Treasury regulations as property for the furnishing of electric energy or gas which is part of a system providing service to the general populace in a service area comprising no more than two contiguous counties. (Treas. Reg. sec. 1.103-8(f) (2) (iii)). In the Revenue Act of 1978, the definition of a facility for the local furnishing of electric energy was modified to also include property for the furnishing of electric energy which is part of a system which provides electric energy to the general populace in a service area comprising no more than a city and one contiguous county.

Issue

The issue is whether the definition of a facility for the local furnishing of gas should be amended to include a facility for the furnishing of gas which is part of a system which provides service to the general populace in an area comprising no more than two contiguous counties or a city and one contiguous county.

Explanation of the bill

The bill provides that the local furnishing of gas from a facility would include the furnishing solely within the area comprising of a city and one contiguous county. Under the bill, tax-exempt financing would be made available in the case of a facility for the furnishing of gas (which otherwise meets the requirements of Code sec. 103) provided that the service area of the facility comprised no more than two contiguous counties or a county and one contiguous city.

The principal beneficiaries of the bill would be the Brooklyn Union Gas Company and the Consolidated Edison Corporation.

Effective date

The bill would apply to obligations issued after the date of enactment.

Revenue effect

It is estimated that this bill would reduce budget receipts by $2 million in fiscal year 1981, $4 million in 1982, $8 million in 1983, $11 million in 1984, and $14 million in 1985.

8. S. 2757—Senators Bentsen, Stevenson, Heinz, and Danforth

Taxation of Export Trading Companies

Present law

Domestic International Sales Corporation (DISC)

Under present law, a DISC is allowed to defer an incremental portion of its export income. This export income includes sales, investment, and services income which result from certain defined export operations of the DISC. With respect to services, this deferrable export income can be for: (1) services related and subsidiary to the sale or other disposition of export property by the DISC, (2) engineering or architectural services for foreign construction projects, or (3) managerial services which further the production of export receipts for the DISC. Income from other services, irrespective of its relationship to export income, is not deferrable export income under the DISC provisions.

Under present law, not all corporations are eligible to be treated as DISCs. Financial institutions, including banks and organizations carrying on banking activities, are not eligible to be DISCs.

Subchapter S corporations

In order for a corporation to qualify as a subchapter S corporation, it must meet several criteria. One of these criteria is that the subchapter S corporation may not have any corporate shareholders during the taxable year. If any of the subchapter S corporation's stock is acquired by a corporation during the taxable year, its subchapter S status is terminated for that year and all future years. However, in the fifth year (or earlier year if the Commissioner consents) following the year of termination, the corporation may re-elect subchapter S status if it meets the eligibility requirements for such year.

Another subchapter S requirement that must be met under present law is that the corporation cannot have more than 80 percent of its gross receipts from foreign sources. Failure to meet this requirement will also result in termination of Subchapter S status.

Background

This bill contains the tax provisions that relate to the companion bill, the Export Trading Company Act of 1980 (S. 2718), which was reported (S. Rept. No. 96–735) by the Senate Committee on Banking, Housing and Urban Affairs on May 15, 1980. The Act is intended to increase U.S. exports of products and services by encouraging export trade services to U.S. producers and suppliers. The Act states that, if exporters are to be successful in promoting U.S. exports, they must be able to draw on the resources, expertise, and knowledge of the U.S. banking system. The principal means by which the bill (S. 2718) attempts to accomplish this end is to amend the banking laws of the United States to allow banks to hold voting stock in an export trading company.

Issues

The issues presented by this bill are:

(1) Whether a banking organization which invests in an export trading company should be allowed to be a DISC;

(2) Whether the category of deferrable DISC income should be expanded to include income from the export of certain U.S. services and the performance of services which facilitate the export of U.S. goods and services;

(3) Whether subchapter S corporations which also qualify as export trading companies should be exempt from the requirements that subchapter S corporations may not have corporate shareholders and cannot have more than 80 percent of their gross receipts from foreign sources.

Explanation of the bill

Domestic International Sales Corporation

In the case of a corporation which is both a DISC and an export trading company,[1] the bill expands the category of deferrable DISC income to include the export of "services produced in the United States" and "export trade services". "Services produced in the United States" are defined in the companion bill (sec. 103(a)(3)) as consulting, management, amusement, etc., services where at least half of the income is attributable to U.S. citizens or is otherwise attributable to the United States. "Export trade services" are defined in the companion bill (sec. 103(a)(4)) as consulting, marketing, financing, etc., activities which facilitate the export of goods or services produced in the United States. Essentially, the bill would allow most, if not all, of the export related activities and services of the dual status corporation to be treated as deferrable DISC income, even if the activities or services are performed in the United States.

The bill would also allow a banking organization which invests in the voting stock of an export trading company to be eligible to be treated as a DISC. The export financing activities of such an organization could qualify as deferrable DISC income. (The expansion of the DISC provisions to include banks and income from banking activities is intended to augment the provisions of the companion bill, S. 2718, which attempts to make banking facilities more available to export trading companies in order to increase their export operations.)

The bill also directs the Secretary of Commerce to prepare and disseminate information to exporters on the advantages and disadvantages of establishing a DISC.

Subchapter S corporations

The bill would allow an export trading company with corporate shareholders to qualify as a subchapter S corporation as long as the corporate shareholders are also subchapter S corporations.

---

[1] Under the companion bill (S. 2718), an export trading company includes any corporation which exports or facilitates the export of U.S. goods and services.

Also, for corporations that are both subchapter S corporations and export trading companies, the bill eliminates the requirement that a subchapter S corporation cannot have more than 80 percent of its gross receipts from foreign sources. (This is intended to allow such a dual status corporation to maximize its export activities without jeopardizing its subchapter S status.)

Effective date

The provisions of the bill would apply to taxable years beginning after December 31, 1980.

Revenue effect

The Department of Treasury has estimated that the bill would reduce calendar year 1981 liabilities by $300 to $700 million.

9. S. 2766—Senator Gravel

Tax Exemption for Industrial Development Bonds for Facilities the Primary Purpose of Which is the Generating of Hydroelectric Power

Present law

Under present law, interest on State and local government obligations is generally exempt from Federal income tax. However, since 1968, tax exemption has been denied to State and local government issues of industrial development bonds (IDBs). A State or local government bond is an IDB if (1) all or a major portion of the proceeds of the issue are to be used in any trade or business of a person other than a State or local government or tax-exempt organization, and (2) payment of principal or interest is secured by an interest in, or derived from payments with respect to, property or borrowed money used in a trade or business.

An exception to the denial of tax exemption for interest of IDBs applies in the case of IDBs which are used to provide exempt activity facilities. Such facilities include qualified hydroelectric generating facilities (Code sec. 103(b)(4)(H)).

Under this provision, tax-exempt IDBs may be used to provide (1) equipment for generating electric energy from water, and (2) structures for housing such equipment, fish passageways, and dam rehabilitation property, where four conditions are satisfied. First, such facilities must be owned for tax purposes by a State or local governmental unit. Second, such facilities must be located at the site of an existing dam or at a site which does not involve the impoundment of water. Third, the installed generating capacity of the generating equipment may not exceed 125 megawatts. Finally, the output of the facility must be available for use by members of the general public. In the case of a facility with an installed capacity of more than 25 megawatts but less than 125 megawatts, only a portion of the cost of the facility may be provided with tax-exempt IDBs.

The exception for qualified hydroelectric generating facilities was enacted as part of the Crude Oil Windfall Profit Tax Act of 1980. That Act, as originally passed by the Senate, would have allowed the use of tax-exempt financing for facilities the primary function of which is the generating of hydroelectric power, except for existing facilities whose construction began before October 25, 1979, and whose installed capacity is more than 25 megawatts. Thus, the Senate version of the Act would have allowed tax-exempt financing for all new hydroelectric dams, for the installation of qualifying property at and the rehabilitation of existing dams which would have an installed generating capacity of less than 25 megawatts, and for qualifying property at a site which did not involve the impoundment of water. The Senate amendment did not, however, allow the use of tax-exempt financing for "pumped storage" facilities. In the conference on that Act, the provisions of the Senate amendment dealing with new dams were deleted.

Issue

The issue is whether tax-exempt IDBs should be allowed to be used to finance all hydroelectric generating facilities.

Explanation of the bill

The bill provides that interest on IDBs used to provide facilities the primary purpose of which is the generation of hydrcelectric power would be exempt from Federal income taxation.

(It is understood that the sponsor of the bill intends that the hydroelectric facilities covered by the bill would automatically meet the public purpose requirement whether or not the output of the facility is made available for use by members of the general public.)

Effective date

The bill would apply to obligations issued after the date of enactment.

Revenue effect

It is estimated that this bill would reduce budget receipts by $20 million in fiscal year 1981, $40 million in 1982, $70 million in 1983, $100 million in 1984, and $140 million in 1985. (This assumes that "pumped storage" facilities are not covered by the bill.)

10. S. 2783—Senators Wallop and Garn

Definition of Shale Oil Equipment for the Energy Investment Credit

Present law

In addition to the generally applicable 10-percent investment tax credit, the Energy Tax Act of 1978 provided a 10-percent energy investment credit for shale oil equipment (Code sec. 48(l)(7)). The latter credit is generally available for property placed in service and expenditures incurred through December 31, 1982. In addition, the energy investment credit for shale oil equipment is available after 1982 and before 1991 where the following specified affirmative commitments are undertaken with respect to qualified property that involves long-term projects: (1) all engineering studies for the project have been completed, and all Federal, State, and local environmental and construction permits have been applied for, prior to 1983 and (2) binding contracts have been made prior to 1986 to acquire or construct at least 50 percent of all equipment that is designed especially for the project (Code sec. 46(a)(2)(C)(iii)).

The term "shale oil equipment" means equipment for producing or extracting kerogen from oil shale. (Kerogen is the liquid hydrocarbon extracted from sedimentary rock known as oil shale, and is referred to as shale oil.) The term "shale oil equipment" does not include equipment for hydrogeneration, refining, or other processes subsequent to retorting. (Retorting is the process of extracting kerogen from oil shale; hydrogenation is a post-retort process, whereby pressurized kerogen reacts with hydrogen gas in the presence of a catalyst for the purpose of purifying the kerogen. Prior to hydrogenation, shale oil is a viscous, and frequently impure, liquid. As such, it generally is not of pipeline quality.) Shale oil equipment includes such equipment involved in either surface or *in situ* processes. In the latter instance, shale oil equipment includes that used to create the underground cavity. In either case, equipment for supplying water, and for treating and handling spent shale rock, is included in the definition of shale oil equipment.

Also, under present law, a deduction for percentage depletion is allowed for 15 percent of the gross income from the extraction of oil shale. For this purpose, gross income includes any increment in value through the retorting stage, but does not include any increment in value attributable to hydrogenation, refining, or any other process subsequent to retorting (Code secs. 613(b)(2)(b) and (c)(4)(H)).

Issue

The issue is whether the definition of shale oil equipment which is eligible for the additional energy investment credit should be extended to include property used for hydrogenation (or similar processes) subsequent to retorting.

Explanation of the bill

The bill would extend the definition of shale oil equipment for purposes of the energy investment credit to include equipment used in hydrogenation or similar processes subsequent to retorting. However, the bill would not expand the definition of shale oil equipment to equipment used to refine shale oil.

Effective date

The bill would apply to periods after December 31, 1980.

Revenue effect

It is estimated that this bill would reduce fiscal year budget receipts by less than $5 million in 1981, $9 million in 1982, $31 million in 1983, $52 million in 1984, and $72 million in 1985.

Prior Congressional consideration

During the 94th Congress, Title XX of the Tax Reform Act of 1976, as reported by the Senate Finance Committee and passed by the Senate (S. Rept. No. 94–938, 94th Cong., 2d Sess. 568–569 (1976)), and H.R. 6860, as reported by the Senate Finance Committee, would have allowed an increased investment credit of 12 percent for shale oil conversion equipment. The credit would have applied to equipment for purifying kerogen. Title XX was not included in the Tax Reform Act of 1976.

11. S. 2784—Senator Gravel

Effective Date of the Energy Investment Credit for Coke Ovens

Present law

The Energy Tax Act of 1978 provided an additional 10-percent investment credit for certain alternative energy property effective for periods after September 30, 1978. As enacted, that Act specifically excluded oil and gas equipment, including that equipment used to produce coke or coke gas, from the new energy investment credit. However, in the consideration of that Act, an amendment was added on the Senate floor that would have allowed the energy investment credit for this type of equipment. This amendment was deleted from the Act by the Conference Committee.

The Crude Oil Windfall Profit Tax of 1980 made equipment used to produce coke or coke gas eligible for the energy investment credit. This extension was effective for periods after December 31, 1979. The extension covers expenditures for new coke ovens and costs incurred in the reconstruction or rehabilitation of existing coke ovens to produce coke and coke gas for use as a fuel or feedstock. In addition, qualifying equipment includes required pollution control equipment and related on site equipment to handle, store, and prepare coal for use in coke ovens.

Issue

The issue is whether the energy investment credit for coke ovens and related expenditures should be available with respect to qualifying investments made after September 30, 1978 and before 1980.

Explanation of the bill

The bill would make the provisions contained in the Crude Oil Windfall Profit Tax Act of 1980 with respect to coke ovens and related expenditures effective for qualifying investments made after September 30, 1978. This is the effective date applicable to the energy credit for alternative energy property investments under the Energy Tax Act of 1978.

Effective date

The change in the eective date would become effective on the date of enactment.

Revenue effect

It is estimated that the bill will reduce budget receipts by $50 million in fiscal year 1981, $3 million in 1982, and an insignificant amount thereafter. (This estimate assumes enactment after September 15, 1980.)

○